2

Taxable Wages, Salary, and Other Compensation

Except for tax-free fringe benefits (*see* Chapter 3), practically everything you receive for your work or services is taxed, whether paid in cash, property, or services. Your employer will generally report your taxable compensation on Form W-2 and other information returns, such as Form 1099 for certain retirement payments and compensatory distributions of securities. Do not reduce the amount you report on your return by withholdings for income taxes, Social Security taxes, union dues, or U.S. Savings Bond purchases. Your Form W-2 does not include in taxable pay your qualifying salary-reduction contributions to a retirement plan, although the amount may be shown on the form.

Attach Copy B of Form W-2 to your return; do not attach Form 1099.

Unemployment benefits are fully taxable. The benefits are reported to the IRS on Form 1099-G. You do not have to attach your copy of Form 1099-G to your return.

	***See* ¶**
Reporting Compensation	
Salary and Wage Income	2.1
Year-End Paychecks	2.2
Pay Received in Property Is Taxed	2.3
Gifts From Employers	2.4
When Commissions Are Taxed	2.5
Unemployment Benefits Are Taxable	2.6
Strike Pay Benefits and Penalties	2.7
Deferring Tax on Pay	2.8
Did You Return Income Received in a Prior Year?	2.9
Waiver of Executor's and Trustee's Commissions	2.10
Disability and Workers' Compensation	
Sick Pay Is Taxable	2.11
Workers' Compensation Is Tax Free	2.12
Employer and Federal Government Disability Pensions	2.13
Pay Plans for Executives	
Deferred Pay Plans	2.14
Insurance Plans May Be Tax Free	2.15
Stock Appreciation Rights (SARs)	2.16
Stock Options and Restricted Stock	2.17
Educational Benefits for Employees' Children	2.18

Also refer to these related subjects:

A Sideline Business or Hobby?	Chapter 40
How To Treat Your Pay:	
For Members of the Armed Forces	Chapter 35
For Citizens Working Abroad	Chapter 36
For Aliens	Chapter 1

Key to Your Form W-2

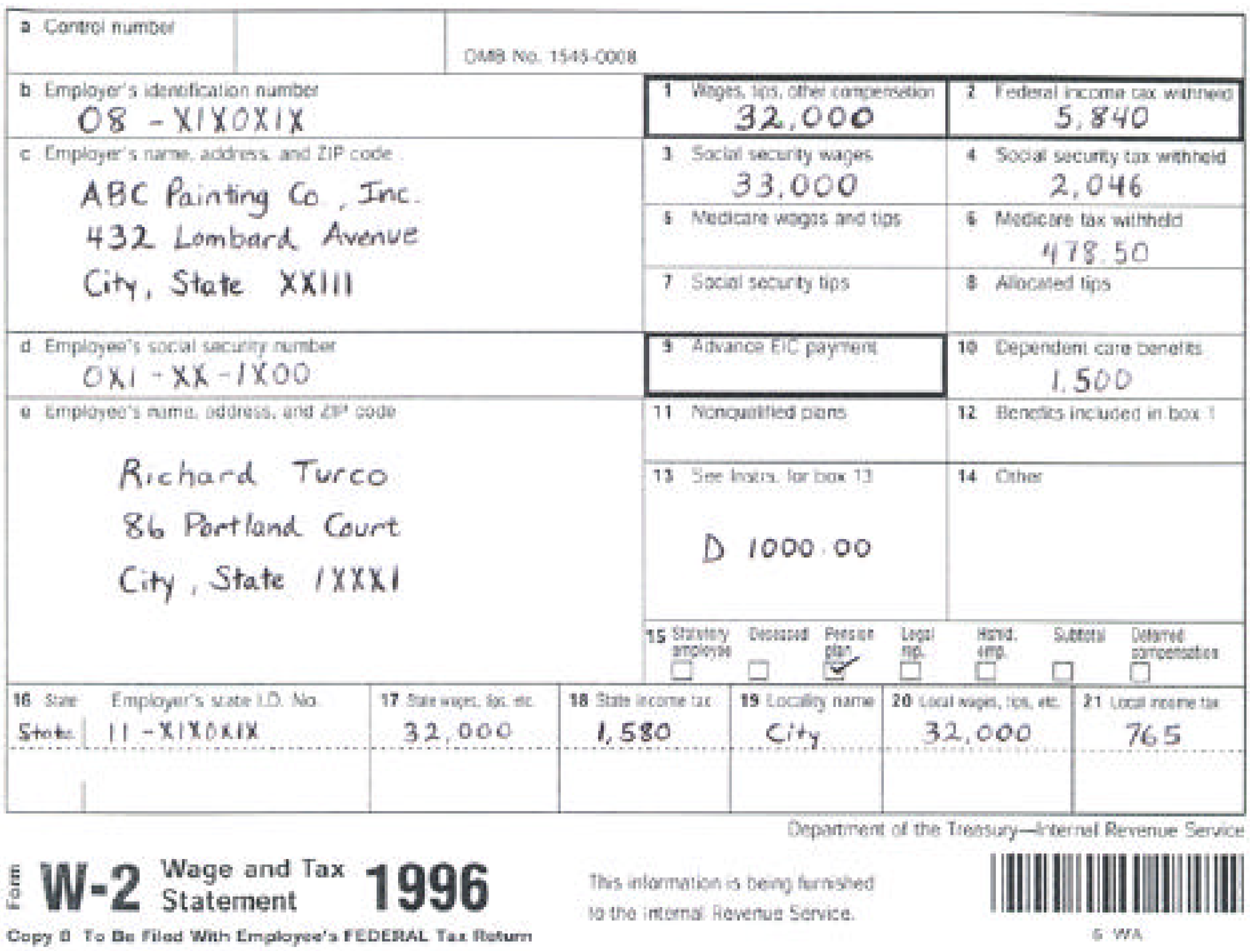
Amount In—	*What You Should Know—*
Box 1	***Taxable wages and tips.*** Your taxable wages and tips are listed in Box 1. In Box 12, your employer lists the amount of taxable fringe benefits that have been included in Box 1 as other compensation. The value of tax-free fringe benefits is not shown on Form W-2. Mileage or per diem travel allowances will not be reported in Box 1 as taxable wages unless they exceed the IRS rate. *See* Box 13. Do not decrease the amount shown in Box 1 by the amount your employer withholds for income taxes, Social Security taxes, disability insurance payments, hospitalization insurance premiums, U.S. Savings Bonds, union dues, or payments to a creditor who has attached your salary. Box 1 does not include salary reduction contributions to a retirement plan. Compensation shown in Box 1 must be reported on Line 7 of Form 1040 or 1040A, or Line 1of Form 1040EZ.
Box 2	***Federal tax withholdings.*** This is the amount of federal income tax withheld from your pay. Enter the amount on Line 52, Form 1040, Line 29a, Form 1040A, or on Line 7, Form 1040EZ. If the withheld amount plus your estimated tax installments exceed your tax liability, you are entitled to a refund for the excess payments.
Boxes 3, 4, and 7	***Social Security withholdings.*** Withholdings for Social Security coverage are at a rate of 6.20% on up to $62,700 of 1996 wages and tips. If your wages were $62,700 or more, Box 4 should show the maximum tax of $3,887.40. If you worked for more than one employer, and a total of more than $3,887.40 was withheld for Social Security taxes, you claim the excess as a tax payment on your tax return; *see* ¶26.10. Wages subject to Social Security withholdings are shown in Box 3. Elective deferrals to a 401(k) plan are included; Social Security withholding applies, although the deferrals are not subject to income tax and are not included in Box 1. Tips you reported to your employer are shown separately in Box 7. The total of Boxes 3 and 7 should not exceed $62,700.
Boxes 5–6	***Medicare tax withholdings.*** Wages and tips subject to Social Security tax (Boxes 3 and 7) are also subject to a 1.45% Medicare tax, except that there is no wage base limit for Medicare tax. Thus, the Medicare wages shown in Box 5 are not limited to the $62,700 maximum for Box 3. For example, if your wages were $100,000, the amount shown in Box 3 (Social Security wages) would be $62,700, but in Box 5, the full $100,000 would be reported. In Box 6, total Medicare withholdings are reported. On wages of $100,000, the Medicare tax would be $1,450 (1.45% × $100,000).
Box 8	***Allocated tips.*** If you worked in a restaurant employing at least 10 people, your employer will report in Box 8 your share of 8% of gross receipts unless you reported tips at least equal to that share (¶26.8). The amount shown here is not included in Box 1 wages, but you must add it to wages on Line 7 of Form 1040; you cannot file Form 1040A or 1040EZ.
Box 9	***Advance earned income payment.*** If you filed a Form W-5 asking for a part of the credit to be added to your wages, the amount of the advance is shown in Box 9. You report the advance as a tax liability when you file Form 1040 or 1040A. *See* Chapter 25 for details on claiming the earned income credit for 1996, and for advanced earned income payments.
Box 10	***Dependent care benefits.*** Reimbursements from your employer for dependent care expenses and the value of employer-provided care services under a qualifying plan (¶3.7) are included in Box 10. Amounts in excess of $5,000 are also included as taxable wages in Boxes 1, 3, and 5. Generally, amounts up to $5,000 are tax free, but you must determine the amount of the exclusion on Form 2441 if you file Form 1040, or on Schedule 2 if you file Form 1040A. The tax-free amount reduces expenses eligible for the dependent care credit; *see* Chapter 25.
Box 11	***Nonqualified plan distributions.*** Distributions shown in Box 11 are from a nonqualified deferred compensation plan, or a Section 457 plan (¶7.21). Do not report these distributions separately since they have already been included as taxable wages in Box 1.
Box 12	***Taxable fringe benefits.*** If you received taxable fringe benefits, your employer shows the amount in Box 12 unless it is reportable in Box 10 or Box 13. For example, the taxable value of using a company car for personal trips (¶3.5), may be included in Box 12. Do not separately report the Box 12 amount as income, since it has already been included in Box 1 as taxable wages.

Key to Your Form W-2

Amount In—	*What You Should Know—*
Box 13	In Box 13, your employer identifies various fringe benefits you received and certain other items by using IRS codes to label each item. No more than three codes should be entered. If you have more than three Box 13 items, the additional items should be shown on a separate Form W-2. ***Elective deferrals to retirement plans.*** If you made elective salary deferrals to an employer retirement plan, Box 15, "deferred compensation," will be checked and your contribution (including any excess over the annual deferral limit) is shown in Box 13. Deferrals to a 401(k) plan (¶7.18) should be labeled with Code D. For example, if you made contributions of $4,500 to a 401(k) plan, your employer would enter D 4500 in Box 13. Code E is used for deferrals to a 403(b) tax-sheltered annuity plan (¶7.20), Code F for deferrals to a simplified employee pension (¶8.17), Code G for deferrals to a Section 457 plan (¶7.21), and Code H for contributions to a pension plan created before June 25, 1959, and funded only by employee contributions. If you participated in more than one plan, the total tax-free deferral for 1996 is $9,500. For 403(b) plans, the limit may in certain cases be $12,500 (¶7.20). Deferrals in excess of the limit must be reported as wages on Line 7 of Form 1040 or Form 1040A (Form 1040EZ may not be used); the excess is not included in Box 1 wages. ***Travel allowance reimbursements.*** If you received a flat mileage allowance from your employer for business trips (¶20.33); or a per diem travel allowance to cover meals, lodging, and incidentals (¶20.32); and the allowance exceeded the IRS rate, the amount up to the IRS rate (the nontaxable portion) is shown in Box 13 using Code L. Do not separately report this amount as income. If you did not substantiate the excess over the IRS rates, that excess is included as taxable wages in Box 1. ***Group-term life insurance over $50,000.*** The cost of coverage over $50,000 is taxable. It is shown in Box 13 using Code C. It is also included in Box 1 wages, Box 3 Social Security wages, and Box 5 Medicare wages and tips. If you are a retiree or other former employee who received group-term coverage over $50,000, any uncollected Social Security tax is shown using Code M; and uncollected Medicare tax, using Code N. The uncollected amount must be reported on Form 1040 in the section for "Other Taxes"; include it on the line for your "total tax" and write "uncollected tax" next to it. ***Nontaxable sick pay.*** If you contributed to a sick pay plan, an allocable portion of benefits received is tax free and is shown using Code J. ***Uncollected Social Security and Medicare taxes on tips.*** If your employer could not withhold sufficient Social Security on tips, the uncollected amount is shown using Code A. For uncollected Medicare tax, Code B is used. This amount must be reported on Form 1040 in the section for "Other Taxes"; include the amount on the line for your "total tax" and write "uncollected tax" next to it. ***Excess golden parachute payments.*** If you received an "excess parachute payment" upon a change in company control, Code K identifies the 20% penalty tax that you must pay on the excess payment. The employer should have withheld this amount and included it in Box 2 federal income tax withholdings. The penalty tax must be reported on Form 1040 in the section for "other taxes," on the line for "total tax."
Box 14	***Miscellaneous payments.*** Your employer may use Box 14 to report payments such as union dues, educational assistance, health insurance premiums, or voluntary after-tax contributions to profit-sharing or pension plans.
Box 15	In Box 15 your employer identifies the following important tax information: ***Statutory employee.*** If this box is checked you get a tax break. You report your wage income and deductible job expenses on Schedule C. This treatment allows job expenses to avoid the 2% adjusted gross income (AGI) floor on Schedule A. *See* ¶40.5 for further details. Your earnings are not subject to income tax withholding, but are subject to Social Security and Medicare taxes. ***Pension plan.*** If the box "pension plan" is checked, this indicates that you were an active participant in an employer plan at some point during the year. As an active participant, you may be unable to make deductible IRA contributions; IRA deductions start to phase out if your AGI exceeds $25,000 and you are single, or $40,000 and you are married filing jointly; *see* Chapter 8. ***Household employee.*** The "Hshld. emp." box will be checked if you worked in the employer's home as a baby-sitter, housekeeper, cook, or butler, or you did similar household work. ***Deferred compensation.*** The box "deferred compensation" is checked if you made salary deferrals to a 401(k) plan (¶7.18), tax-sheltered 403(b) annuity (¶7.20), or simplified employee pension plan (¶8.17). In Box 13, the employer lists the total elective deferrals to these plans.
Boxes 18 and 21	***State and local taxes.*** If you itemize deductions on Schedule A, do not forget to deduct the state and local tax withholdings shown in Boxes 18 and 21. These amounts offset tax liability on your state and local tax returns.

Sample Form W-2

You should receive your Form W-2 for 1996 from your employer by January 31, 1997.


a Control number

OMB No. 1545-0008

b Employer's identification number
08 - XIXOXIX

c Employer's name, address, and ZIP code
ABC Painting Co, Inc.
432 Lombard Avenue
City, State XXIII

d Employee's social security number
OXI - XX - IXOO

e Employee's name, address, and ZIP code
Richard Turco
86 Portland Court
City, State IXXXI

1 Wages, tips, other compensation 32,000	2 Federal income tax withheld 5,840
3 Social security wages 33,000	4 Social security tax withheld 2,046
5 Medicare wages and tips	6 Medicare tax withheld 478.50
7 Social security tips	8 Allocated tips
9 Advance EIC payment	10 Dependent care benefits 1,500
11 Nonqualified plans	12 Benefits included in box 1
13 See Instrs. for box 13 D 1000.00	14 Other

15 Statutory employee ☐ Deceased ☐ Pension plan ☑ Legal rep. ☐ Hshld. emp. ☐ Subtotal ☐ Deferred compensation ☐

16 State	Employer's state I.D. No.	17 State wages, tips, etc.	18 State income tax	19 Locality name	20 Local wages, tips, etc.	21 Local income tax
State	11 - XIXOXIX	32,000	1,580	City	32,000	765

Department of the Treasury—Internal Revenue Service

Form **W-2** Wage and Tax Statement **1996**

This information is being furnished to the Internal Revenue Service.

Copy B To Be Filed With Employee's FEDERAL Tax Return

6 WA

Reporting Compensation

¶2.1 Salary and Wage Income

The key to reporting your pay is Form W-2, sent to you by your employer. It lists your taxable wages, which may include not only your regular pay, but also other taxable items, such as taxable fringe benefits. A guide to the important information listed on Form W-2 is on pages 26 and 27.

Your employer reports your taxable pay under a simple rule. Unless the item is specifically exempt from tax, you are taxed on practically everything you receive for your work whether paid in cash, property, or services. Taxed pay includes:

Back pay	Honoraria
Bonuses	Jury fees
Commissions	Salaries
Director's fees	Severance pay
Sick pay	Dismissal pay
Employee prizes or awards	Tips
Expense allowances or reimbursements under nonaccountable plans	Vacation pay
	Wages

The items that the law specifically excludes from tax are discussed in Chapter 3. The most common tax-free benefits are employer-paid premiums for health and accident plans and certain group-term life insurance plans for coverage up to $50,000.

CAUTION

Severance Pay Taxable

You must pay tax on severance pay received upon losing a job. The severance pay is taxable even if you signed a waiver releasing your former employer from potential future damage claims. The waiver does not change the nature of the payments from taxable pay to tax-free personal injury damages; *see* ¶12.10.

Withholdings for retirement plans. Amounts withheld from wages as your contribution to your pension or profit-sharing account are generally taxable unless they are tax-deferred under the limits allowed for Section 401(k) plans (¶7.18), simplified employee pension plans (¶8.17), or tax-sheltered annuity plans (¶7.20). Tax-deferred amounts are reported in Box 13 of Form W-2. Courts have held that amounts withheld from the pay of both U.S. Civil Service employees and city and county civil service employees are taxable to the employees.

Wages withheld for compulsory forfeitable contributions to a nonqualified pension plan are not taxable if these conditions exist:

1. The contribution is forfeited if employment is terminated prior to death or retirement.
2. The plan does not provide for a refund of employee contributions and, in the administration of the plan, no refund will be made. Where only part of the contribution is subject to forfeiture, the amount of withheld contribution not subject to forfeiture is taxable income.

You should check with your employer to determine the status of your contributions.

Assigning your pay. You may not avoid tax on income you earned by assigning the right to payment to another person. For example, you report earnings donated by you but paid directly by your employer to a charity. You may claim a contribution deduction for the donation; *see* Chapter 14. The IRS allowed an exception for doctors working in a clinic. They were required to assign to a foundation all fees derived from treating patients with limited income (teaching cases). The fees were not taxable.

Salary advances. Salary paid in advance for services to be rendered in the future is generally taxable in the year received if it is subject to your free and unrestricted use.

Child's wages. A parent is not taxed on wages paid for a child's services even if payment is made to the parent. However, a parent is taxed on income from work contracted for by the parent even if the child assists in the labor. For example, a parent whose children helped her with part-time work at home claimed that the children should be taxed on 70% of the income since they did 70% of the work. The IRS claimed that the parent was taxable on all the income because she, not the children, was the true earner, and the Tax Court agreed. Although the company knew that the children were doing part of the work, it had no agreement with them.

Employee leave-sharing plan. Some companies allow employees to contribute their unused leave into a "leave fund" for use by other employees who have suffered medical emergencies. If you use up your regular leave and benefit from additional leave that has been donated to the plan, the benefit is taxable and will be reported as wages on Form W-2.

"Golden parachute" payments. Golden parachute arrangements are agreements to pay key employees additional compensation upon a change in company control. If you receive such a payment, part of it may be deemed to be an "excess payment" under a complex formula in the law. You must pay a 20% penalty tax on the "excess" amount in addition to regular income tax on the total. The excess amount should be identified on Form W-2 with Code K in Box 13; *see* the Key to Your Form W-2 at the beginning of this chapter.

If the golden parachute payment was reported on Form 1099-MISC, it will be included in Box 7 as non-employee compensation. If you are self-employed, report the total compensation on Schedule C (¶40.5) and compute self-employment tax on Schedule SE (¶46.3).

Any "excess parachute payment" should be separately labeled in Box 7 of Form 1099-MISC. Multiply the excess payment by 20% and report it in the section of Form 1040 for "other taxes," on the line for "total tax."

¶2.2 Year-End Paychecks

As an employee, you use the cash basis method of accounting. This means that you report all income items in the year they are actually received and deduct expenses in the year you pay them.

You are also subject to the "constructive receipt rule," which requires you to report income not actually received but which has been credited to your account, subject to your control, or put aside for you. Thus, if you received a paycheck on December 31, 1996, you must report the pay on your 1996 return, even though you do not cash or deposit it to your account until 1997. This is true even if you receive the check after banking hours and cannot cash or deposit it until the next year.

If your employer does not have funds in the bank and asks you to hold the check before depositing it, you do not have taxable income until the check is cashed. If pay for services rendered in 1996 is paid by check dated for 1997, the pay is taxable in 1997.

The IRS has ruled that an employee who is not at home on December 31 to take delivery of a check sent by certified mail must still report the check in that year. However, where an employee was not at home to take certified mail delivery of a year-end check that she did not expect to receive until the next year, the Tax Court held that the funds were taxable when received in the following year.

¶2.3 Pay Received in Property Is Taxed

Your employer may pay you with property instead of cash. You report the fair market value of the property as wages.

EXAMPLE

For consulting services rendered, Kate Chong receives a check for $10,000 and property having a fair market value of $5,000. She reports $15,000 as wages.

If you receive your company's stock as payment for your services, you include the value of the stock as pay in the year you receive it. However, if the stock is nontransferable or subject to substantial risk of forfeiture, you do not have to include its value as pay until the restrictions no longer apply; *see* ¶2.17. You must report dividends on the restricted stock in the year you receive the income.

If you receive your employer's note which has a fair market value, you are taxed on the value of the note less what it would cost you to discount it. If the note bears interest, report the full face value. But do not report income if the note has no fair market value. Report income on the note only when payments are made on it.

A debt cancelled by an employer is taxable income.

A salesman employed by a dealer has taxable income on receipt of "prize points" redeemable for merchandise from a distributor.

¶2.4 Gifts From Employers

A payment may be called a gift but still be taxable income. Any payment made in recognition of past services or in anticipation of future services or benefits is taxable even if the employer is not obligated to make the payment. Exceptions for employee achievement awards are discussed at ¶3.10.

To prove a gift is tax free, you must show that the employer acted with pure and unselfish motives of affection, admiration, or charity. This is difficult to do, given the employer-employee relationship.

A gift of stock by majority stockholders to key employees has been held to be taxable income.

¶2.5 When Commissions Are Taxed

Earned commissions are taxable in the year they are credited to your account and subject to your drawing, whether or not you actually draw them.

On your 1996 tax return, you do not report commissions which were earned in 1996 but which cannot be computed or collected until a later year.

EXAMPLE

Arno Jeffers earns commissions based on a percentage of the profits from realty sales. In 1996 he draws $10,000 from his account. However, at the end of 1996 the full amount of his commissions is unknown because profits for the year have not been figured. In January 1997, his 1996 commissions are computed to be $15,000, and the $5,000 balance is paid to him. The $5,000 is taxable in 1997 even though earned in 1996.

You may not postpone tax on earned commissions credited to your account in 1996 by not drawing them until 1997 or a later year. However, where a portion of earned commissions is not withdrawn because your employer is holding it to cover future expenses, you are not taxed on the amount withheld.

Advances against unearned commissions. Under standard insurance industry practice, an agent who sells a policy does not earn commissions until premiums are received by the insurance company. However, the company may issue a cash advance on the commissions before the premiums are received. Agents have claimed that they may defer reporting the income until the year the premiums are earned. The IRS, recognizing that in practice companies rarely demand repayment, requires that advances be included in income in the year received if the agent has full control over the advanced funds. A repayment of unearned commissions in a later year is deducted on Schedule A; *see* ¶2.9.

Salespeople have been taxed on commissions received on property bought for their personal use. In one case, an insurance agent was taxed on commissions paid to him on his purchase of an insurance policy. In another case, a real estate agent was taxed on commissions he received on his purchase of land. A salesman was also taxed for commissions waived on policies he sold to friends, relatives, and employees.

Kickback of commission. An insurance agent's kickback of his or her commission is taxable where agents may not under local law give rebates or kickbacks of premiums to their clients. The commissions are income and may not be offset with a business expense deduction; illegal kickbacks may not be deducted.

However, in one case, a federal appeals court allowed an insurance broker to avoid tax when he did not charge clients the basic first-year commission. The clients paid the broker the *net* premium (gross premium *less* the commission), which he remitted to the insurance company. The IRS and Tax Court held that the commissions were taxable despite the broker's voluntary waiver of his right to them. He could not deduct them because his discount scheme violated state anti-rebate law (Oklahoma). On appeal, the broker won. The Tenth Circuit Court of Appeals held that since the broker never had any right to commissions under the terms of the contracts he structured with his clients, he was not taxed on the commissions. The court cautioned that if the broker had remitted the full premium (including commission) to the insurance company and then reimbursed the client after having received the commission from the company, the commission probably would have been taxable.

¶2.6 Unemployment Benefits Are Taxable

All unemployment benefits you receive in 1996 from a state agency or the federal government are treated as taxable income. You should receive Form 1099-G, showing the amount of the payments. Report the payments separately from wages on Line 19 of Form 1040, Line 12 of Form 1040A or Line 3 of Form 1040EZ.

Supplemental unemployment benefits paid from company-financed funds are taxable as wages and not reported as unemployment compensation. Such benefits are usually paid under guaranteed annual wage plans made between unions and employers.

Unemployment benefits from a private or union fund to which you voluntarily contribute dues are taxable as "other" income on Form 1040, but only to the extent the benefits exceed your contributions to the fund. Your contributions to the fund are not deductible.

Worker's compensation payments are not taxable; *see* ¶2.12.

Taxable unemployment benefits include federal trade readjustment allowances (1974 Trade Act), airline deregulation benefits (1978 Airline Deregulation Act), and disaster unemployment assistance (1974 Disaster Relief Act).

If you had to repay supplemental unemployment benefits to receive trade readjustment allowances (1974 Trade Act), taxable unemployment benefits are reduced by repayments made in the same year. If you repay the benefits in a later year, the benefits are taxed in the year of receipt and a deduction may be claimed in the later year. If the repayment is $3,000 or less, the deduction is added to your other adjustments to income on Line 30 on page 1 of Form 1040. If the repayment exceeds $3,000, a deduction or a credit may be claimed under the rules of ¶2.9.

¶2.7 Strike Pay Benefits and Penalties

Strike and lockout benefits paid out of regular union dues are taxable as wages unless the payment qualifies as a gift, as discussed below. However, if you have made *voluntary* contributions to a strike fund, benefits you receive from the fund are tax free up to the amount of your contributions and are taxable to the extent they exceed your contributions.

Strike benefits as tax-free gifts. Here are factors indicating that benefits are gifts: Payments are based on individual need; they are paid to both union and nonunion members; and no conditions are imposed on the strikers who receive benefits.

If you receive benefits under conditions by which you are to participate in the strike and the payments are tied to your scale of wages, the benefits are taxable.

EXAMPLE

A striking union pilot claimed that strike benefits were tax-free gifts because they were funded by assessments paid by other union pilots who were not on strike. The IRS and Tax Court held that the benefits were taxable. They were not gifts because they were not motivated by a "detached and disinterested generosity." The union was promoting its own self-interest by giving pilots an incentive to support the strike. The non-striking pilots contributed to the strike fund as an obligation of union membership. The strikers were eligible for benefits only if they agreed to perform any strike activities requested by the union, did not fly for airlines in dispute with the union, and did not take actions that could adversely affect the outcome of the dispute.

Strike pay penalties. Pay penalties charged striking teachers are not deductible. State law may prohibit public school teachers from striking and charge a penalty equal to one day's pay for

each day on strike if they do strike. For example, when striking teachers returned to work after a one-week strike, a penalty of one week's salary was deducted from their pay. Although they did not actually receive pay for the week they worked after the strike, they earned taxable wages. Furthermore, the penalty is not deductible. No deduction is allowed for a fine or penalty paid to a government for the violation of a law.

¶2.8 Deferring Tax on Pay

If you want to avoid current tax on pay, you may contract with your employer to defer pay to future years. To reduce possible IRS opposition, it is advisable to enter into a deferral compensation arrangement before the year in which the services are to be performed; for example, agree in 1997 to defer pay for 1998 services to 1999 or later years. Furthermore, to defer pay to a future period, you must take some risk. You cannot have any control over your deferred pay account. If you are not confident of your employer's ability to pay in the future, you should not enter into a deferred pay plan.

Before agreeing to a deferral arrangement, consider the possibility that if tax rates are raised further, you may be subject to a higher tax on deferred pay than if you had received and paid tax currently on the income.

If IRS tests are met, a trust arrangement, commonly nicknamed a "*rabbi trust*," can be used by an employer to hold deferred pay contributions; *see* ¶2.14.

An employee is not taxed on employer contributions to a qualified cash or deferred arrangement (401(k) plan) even though the employee had the option to take the cash; *see* ¶7.17. Qualified salary reductions under a simplified employee pension plan (SEP) (¶8.17) or tax-sheltered annuity plan (¶7.20) are also not taxed, even though you could have received cash currently.

¶2.9 Did You Return Income Received in a Prior Year?

Did you return income in 1996 such as salary or commissions which you reported in a prior taxable year because it appeared you had an unrestricted right to it in the earlier year? If so, you may deduct the repayment as a miscellaneous itemized deduction. If the repayment exceeds $3,000, the deduction is claimed on Line 27 of Schedule A and is *not* subject to the 2% adjusted gross income (AGI) floor (¶19.1). However, the law is not clear on the issue of whether a deduction of $3,000 or less is subject to the 2% floor; the IRS takes the position that the 2% floor applies.

Repayment of supplemental unemployment benefits. Where repayment is required to qualify for trade readjustment allowances, you may deduct the repayment from gross income. Claim the deduction on Line 30 of Form 1040, and to the left of the line write "subpay TRA." The deduction is allowed even if you do not itemize. If repayment is $3,000 or more, you have the choice of a deduction or claiming a credit based on a recomputation of your tax for the year supplemental unemployment benefits were received, as previously explained.

Repayment of disallowed travel & entertainment expenses. If a "hedge" agreement between you and your company requires you to repay salary or travel and entertainment ("T & E") expenses if they are disallowed to the company by the IRS, you may claim a deduction in the year of repayment. According to the IRS, you may not recalculate your tax for the prior year and claim a tax credit under the rules of Section 1341. However, an appeals court rejected the position taken by the IRS and allowed a tax recomputation under Section 1341 to an executive who returned part of a disallowed salary under the terms of a corporate by-law.

Repayments Exceeding $3,000

If the repayment exceeds $3,000, a special law (Code section 1341) gives this alternative: Instead of claiming an itemized deduction from 1996 income, you may recompute your tax for the prior year as if the income had not been reported. The difference between the actual tax paid in the prior year and the recomputed tax may be claimed as a credit on your 1996 return. The credit is claimed on Line 57 of Form 1040; write next to the line "IRC 1341." If you claim the repayment as a miscellaneous itemized deduction, enter it on Line 27 of Schedule A, where it is *not* subject to the 2% floor. Choose either the credit or the itemized deduction, whichever gives you the larger tax reduction. The Section 1341 credit does not apply to the refund of income arising from the sale of inventory items.

¶2.10 Waiver of Executor's and Trustee's Commissions

Commissions received by an executor for services performed are taxable as compensation. An executor may waive commissions without income or gift tax consequences by giving a principal legatee or devisee a formal waiver of his or her right to commissions within six months after the initial appointment or by not claiming commissions at the time of filing the usual accountings.

The waiver may not be recognized if he or she takes any action that is inconsistent with the waiver. An example of an inconsistent action would be the claiming of an executor's fee as a deduction on an estate, inheritance, or income tax return.

A *bequest* to an executor is tax free if it is not compensation for services.

Disability and Workers' Compensation

¶2.11 Sick Pay Is Taxable

Sick pay is generally taxable as wages unless it qualifies as workers' compensation under the rules of ¶2.12. Payments received under accident or health plans are tax free if you paid the premiums; *see* ¶17.5. Payments from your employer's plan for certain serious permanent injuries are tax free; *see* ¶3.2.

Disability pensions are discussed at ¶2.13.

Sick pay received from your employer is subject to withholding as if it were wages. Sick pay from a third party such as an insurance company is not subject to withholdings unless you request it on Form W-4S.

¶2.12 Workers' Compensation Is Tax Free

You do not pay tax on workers' compensation payments for job-related injuries or illness. However, your employer might continue paying your regular salary but require you to turn over your workers' compensation payments. Then you are taxed on the difference between what was paid to you and what you returned.

EXAMPLE

John Wright was injured while at work and was out of work for two months. His company continues to pay his weekly salary of $475. He also receives workers' compensation of $100 a week from the state, which is tax free. He gives the $100 back to his employer. The balance of $375 a week is considered taxable wages.

To qualify as tax-free workers' compensation, the payments must be made under the authority of a *law* (or regulation having force of a law) that provides compensation for on-the-job injury or illness. Payments made under a labor agreement do *not* qualify as tax-free workers' compensation; *see* the Examples at the end of this section.

CAUTION

Job-Related Injury or Illness

Not all payments for job-related illness or injury qualify as tax-free workers' compensation. Unless the statute or regulation authorizing your disability payment restricts awards to on-the-job injury or illness, your payment is taxable. Even if your payments are in fact based upon job related injury or illness, they are taxed if other individuals can receive payments from the plan for disabilities that are not work related; *see* the following Example.

EXAMPLE

Kane, a federal district judge, suffered from sleep apnea, a condition characterized by a cessation of breathing during sleep, which was aggravated by the stress of his judicial work. He received a retirement disability payment of $65,135.

The payment is taxable because it was paid under a statute which did not specifically require that the payments be for work-related injuries. Here, the federal law under which the judge received his payments provided benefits for all permanent disabilities, whether or not job related.

Effect of workers' compensation on Social Security. In figuring whether Social Security benefits are taxable (¶34.2), workers' compensation that reduces Social Security or equivalent Railroad Retirement benefits is treated as a Social Security (or Railroad Retirement) benefit received during the year. Thus, the workers' compensation may be indirectly subject to tax under ¶34.3.

COURT DECISION

Is Sick Leave Tax-Free Workers' Compensation?

According to the Tax Court, sick leave may qualify as tax-free workers' compensation if it is paid under a specific workers' compensation statute or similar government regulation that authorizes the sick leave payment for job-related injuries or illness. *See* Examples 1, 3, and 4 on the next page.

EXAMPLES

1. A teacher, injured while working, received full salary during a two-year sick leave. She argued that the payments, made under board of education regulations, were similar to workers' compensation and thus tax free. The IRS disagreed; the regulations were not the same as a workers' compensation statute. The Tax Court supported the teacher. Although not made under a workers' compensation statute, the payments were made because of job-related injuries and were authorized by regulations having the force of law.
2. A disabled New York City policeman argued that sick leave payments in 1978 under a union labor contract were tax-free workers' compensation because his disability was work related. However, the IRS, Tax Court, and an appeals court disagreed. The payments were made under a labor contract and not a workers' compensation statute or pursuant to government regulations. Furthermore, even if authorized by a statute or regulations, the officer's sick leave would be taxable since under the labor contract, officers received sick pay whether or not their injury or illness was work related.

   A change in New York City law now qualifies sick leave payments to firefighters and police officers for line–of–duty injuries as tax-free workers' compensation.
3. The IRS, relying on the court decision in Example 2, claimed that a police officer in Lynbrook, N.Y., was subject to tax on line-of-duty disability pay because the payment was under a labor agreement with the Police Benevolent Association (PBA). The Tax Court supported the police officer's claim that the payments were authorized by a specific New York State law requiring full salary for job-related police injuries. The PBA agreement did not affect the officer's rights to those state law payments. Furthermore, Lynbrook treated the case as a workers' compensation claim and in fact received reimbursement for the payments made to the officer from the state workers' compensation board.
4. A Los Angeles sheriff injured on the job retired on disability and, under the Los Angeles workers' compensation law, was allowed to elect sick pay in lieu of the regular workers' compensation amount because the sick pay was larger. The IRS argued that the sheriff had merely received taxable sick pay because he would have received the same amount as sick pay if his injuries had been suffered in a personal accident. However, the Tax Court allowed tax-free treatment. The sick leave was paid under a workers' compensation law that applied solely to work-related injuries. The fact that sick leave may also have been available to other employees under other laws does not mean that it may not be included as an option under a workers' compensation statute.

   The IRS announced that it does not agree with the Tax Court's decision allowing full tax-free treatment. According to the IRS, benefits up to the regular workers' compensation amount should be tax free but excess amounts should be taxed.

¶2.13 Employer and Federal Government Disability Pensions

Disability pensions financed by your employer are reported as wage income unless they are for severe permanent physical injuries that qualify for tax-free treatment under the rules of ¶3.2 or they are tax-free government payments as discussed in this section. Turn to ¶34.7 to see if you may claim a tax credit for the receipt of a disability pension. A credit, subject to income limitations, is allowed for disability payments received while you are under the age of 65 and permanently and totally disabled.

Taxable disability pensions are reported as wages until you reach the minimum retirement age under the employer's plan. After reaching minimum retirement age, payments are reported as a pension under the rules of ¶7.25.

Federal government services. Certain disability pensions from the military or federal government agencies are tax free. Military disability benefits from the Veterans Administration are tax free, as are payments for combat and terrorist attack–related injuries. Other disability pensions for personal injuries or sickness resulting from active service in the armed forces are *taxable* if you joined the service after September 24, 1975.

Military disability payments are tax free if on September 24, 1975, you were entitled to military disability benefits or if on that date you were a member of the armed forces (or reserve unit) of the U.S. or any other country or were under a binding written commitment to become a member. A similar tax-free rule applies to disability pensions from the following government agencies if you were entitled to the payments on September 24, 1975, or were a member of the service (or committed to joining) on that date: The Foreign Service, Public Health Service, or National Oceanic and Atmospheric Administration. The exclusion for pre-September 25, 1975, service applies to disability pensions based upon percentage of disability. However, if a disability pension was based upon years of service, you do not pay tax on the amount that would be received based upon percentage of disability.

Veterans Administration benefits. Disability pensions from the Veterans Administration (now called the Department of Veterans Affairs) are tax free. Military retirees who receive disability benefits from other government sources are not taxed on amounts equal to the benefits they would be entitled to receive from the VA. If you retire from the military and are later given a retroactive award of VA disability benefits, retirement pay during the retroactive period is tax free (other than a lump-sum readjustment payment upon retirement) to the extent of the VA benefit.

Pension based on combat-related injuries. Tax-free treatment applies to payments for combat-related injury or sickness which is incurred as a result of any one of the following activities: (1) as a direct result of armed conflict; (2) while engaged in extra-hazardous service, even if not directly engaged in combat; (3) under conditions

simulating war, including maneuvers or training; or (4) which is caused by an instrumentality of war, such as weapons.

Terrorist attacks. Tax-free treatment applies to a disability pension paid to a civilian U.S. employee for injuries incurred as a direct result of a violent attack which the Secretary of State determines to be a terrorist attack and which occurred while the employee was working for the United States in the performance of official duties outside the United States.

Pay Plans for Executives

¶2.14 Deferred Pay Plans

The major objective of a deferred pay plan is to postpone the tax on pay benefits to a year in which you will be in a lower tax bracket than in the year you provide the services. However, a deferred pay plan is generally not advisable where a projection of future income shows that there probably will be no substantial income decline, and/or the tax bracket differentials will not be wide. An after-tax dollar in hand for current use is preferable to an expectation of a tax saving that may not materialize.

As discussed at ¶2.8, a deferral arrangement will succeed in postponing tax only if there is an element of risk. An employee with control over the pay account will be treated by the IRS as in "constructive receipt," and thus currently taxable on employer contributions.

Rabbi trusts. If IRS tests are met, employer contributions to a "rabbi trust" are not taxed until distributions from the trust are received or made available. The trust must be irrevocable and the trust assets must be subject to the claims of the employer's creditors in the event of insolvency or bankruptcy. Employees and their beneficiaries have only the rights of unsecured creditors; they have no preferred claim on the trust assets. The IRS has created a model rabbi trust agreement that may be relied upon in structuring a plan; the details are in Revenue Procedure 92-64.

Pension and profit-sharing plans. A company qualified pension or profit-sharing plan offers the following benefits: (1) you do not realize current income on your employer's contributions to the plan on your behalf; (2) funds contributed by both your employer and you compound tax free within the plan; (3) if you receive a lump-sum distribution, tax on employer contributions may in certain cases be reduced by a special averaging rule (¶7.4); and, (4) if you receive a lump-sum distribution in company securities, unrealized appreciation on those securities is not taxed until you finally sell the stock.

In plan years starting in 1996, the maximum amount of compensation that can be taken into account for purposes of determining qualified employer plan contributions and benefits is $150,000. The $150,000 limit may be adjusted annually for inflation.

Where you are allowed to choose the type of payout from a qualified plan, make sure that you compare the tax on receiving a lump-sum distribution with the projected tax cost of deferring payments over a period of years or rolling over the distribution to an IRA account; *see* ¶7.3 and ¶7.8. Distributions before age 59½ are generally subject to penalties, but *see* exceptions at ¶7.14.

401(k) plan. If your company has a profit-sharing or stock bonus plan, it has the opportunity to give you additional tax-sheltered pay; *see* ¶7.17. The tax law allows the company to add a cash or deferred pay plan, called a "401(k) plan." If your company permits salary-reduction deferrals to a 401(k) plan, you may be able to make contributions on a pre-tax basis up to the annual limit set by law, which for 1996 was $9,500. However, the limit may be reduced for highly compensated employees in order for the company to satisfy nondiscrimination requirements; *see* ¶7.18.

¶2.15 Insurance Plans May Be Tax Free

Company-financed insurance for employees is a common method of giving additional benefits at low or no tax cost.

Group life insurance. Group insurance plans may furnish not only life insurance protection but also accident and health benefits. Premium costs are low and tax deductible to the company while tax free to you unless you have nonforfeitable rights to permanent life insurance, or, in the case of group-term life insurance, your coverage exceeds $50,000; *see* ¶3.3. Even where your coverage exceeds $50,000, the tax incurred on your employer's premium payment is generally less than what you would have to pay privately for similar insurance.

It may be possible to avoid estate tax on the group policy proceeds if you assign all of your ownership rights in the policy, including the right to convert the policy, and if the beneficiary is other than your estate. Where the policy allows assignment of the conversion right, in addition to all other rights, and state law does not bar the assignment, you are considered to have made a complete assignment of the group insurance for estate tax purposes.

The IRS has ruled that where an employee assigns a group life policy and the value of the employee's interest in the policy cannot be ascertained, there is no taxable gift. This is so where the employer could simply have stopped making payments. However, there is a gift by the employee to the assignee to the extent of premiums paid by the employer. That gift is a present interest qualifying for the $10,000 annual exclusion.

Split-dollar insurance. Where you want more insurance than is provided by a group plan, your company may be able to help you get additional protection through a split-dollar insurance plan. Under the basic split-dollar plan, your employer purchases permanent life insurance on your life and pays the annual premium to the extent of the yearly increases in the cash surrender value of the policy. You pay only the balance of the premium. At your death, your employer

is entitled to part of the proceeds equal to the cash surrender value or any lesser amount equalling the total premiums he or she paid. You have the right to name a beneficiary to receive the remaining proceeds which, under most policies, are substantial compared with the employer's share.

The IRS has ruled that you must report as taxable income an amount equal to the one-year term cost of the declining life insurance protection to which you are entitled, less any portion of the premium provided by you. According to the IRS, there is an additional tax liability to employees under "equity split-dollar plans" that allow the employees to receive the cash surrender value in excess of the premiums paid by the employer. For example, a company paid in a lump sum the premium on a life insurance policy for an executive and it was projected that the cash surrender value would exceed the employer's premium payment in the fourth policy year. The IRS ruled that once the cash surrender value of the policy exceeds the premiums that are returnable to the employer upon the employer's death (or termination of the agreement upon the executive's leaving the company), the employee must report as income the excess cash surrender value. This is in addition to the income realized on the one-year term cost for the declining insurance protection.

¶2.16 Stock Appreciation Rights (SARs)

SARs are a form of cash bonus tied to an increase in the price of employer stock. Each SAR entitles an employee to cash equal to the excess of the fair market value of one share on the date of exercise over the value on the date of the grant of the SAR.

EXAMPLE

When a stock is worth $30 a share, you get 100 SARs exercisable within five years. Two years later, when the stock price increases to $50 a share, you exercise the SAR and receive $2,000. You are taxed when you receive the cash.

CAUTION

Watch SAR Expiration Date

If the rights increase in value, keep a close watch on the expiration date. Do not let them expire before exercise. If you do, not only will you lose income but you will be taxed on income you never received. According to the IRS, an employee who does not exercise the SARs is taxed as if they had been exercised immediately before they expire. The IRS claims that an employee has constructive receipt of income immediately before they expire. At that time, the amount of gain realized from the SARs is fixed because the employee can no longer benefit from future appreciation in value.

An executive may realize taxable income when he or she becomes entitled to the maximum SAR benefit allowed by the company plan. For example, in 1991, when company stock is worth $30, an executive is granted 100 SARs exercisable within five years. By exercising the SARs, the executive may receive cash equal to the appreciation up to $20 per share. If the stock appreciates to $50 per share in 1996, the executive realizes taxable income of $2,000 ($20 per share × 100) in 1996, even if he or she does not exercise the SARs. The reason is that once the stock value appreciated to $50, the maximum SAR benefit of $20 was realized.

Performance shares. The company promises to make an award of stock in the future, at no cost to you, if the company's earnings reach a set level. You are taxed on the receipt of stock (unless the stock is restricted, as discussed in ¶2.17).

¶2.17 Stock Options and Restricted Stock

Executives receiving qualified statutory stock options generally do not incur tax liability either at the time the option is granted or when the option is exercised, although the option spread may be subject to AMT; *see* ¶23.5. Qualified statutory options include incentive stock options and options under an employee stock purchase plan. Receipt of a nonqualified stock option may result in an immediate tax.

Incentive stock options (ISOs). A corporation may provide its executives with incentive stock options to acquire its stock (or the stock of its parent or subsidiaries). For regular income tax purposes, ISOs are not taxed when granted or exercised. The option spread is taxable as capital gain if the stock acquired by the exercise of the option is not sold until more than one year after it was acquired and more than two years after the option was granted. If a corporation grants an executive ISOs to purchase stock valued at over $100,000, the maximum ISO limit for options first exercisable in any one year is $100,000. For other restrictions on ISOs, *see* the terms of your company plan. For AMT tax consequences, *see* ¶23.5.

Employee stock purchase plans. These plans allow employees to buy their company's stock, usually at a discount. The plan must be nondiscriminatory and meet tax law tests on option terms. Options granted under qualified plans are not taxed until the shares acquired are sold. If you do not sell the shares until more than two years have passed since granting of the option, and the stock is held more than one year, gain on the sale is reported as ordinary wage income to the extent the option price was less than the fair market value of the shares when the option was granted. Any excess gain is capital gain; *see* ¶5.2 for the tax rate on net capital gains. For sales before the end of the two-year/one-year holding period, the amount reportable as ordinary wage income is the excess of the value of the shares when the option was exercised over the option price.

Nonqualified stock options. Where a nonqualified option has no ascertainable fair market value, as is generally the case, no income is realized on the receipt of the option. Income is realized when the option is exercised. If a nonqualified stock option has an ascertainable fair market value, the value of the option less any amount paid by the employee is taxable as ordinary wage income in the first year that the employee's right to the option is freely transferable or not subject to a substantial risk of forfeiture. For other details and requirements, *see* IRS regulation Section 1.83–7.

Nonqualified stock options may be granted in addition to or in place of incentive stock options. There are no restrictions on the amount of nonqualified stock options that may be granted.

When sale of stock is treated as grant of option. If company stock is purchased on the basis of the executive's promissory note and he or she is not personally liable, the company can recover only its stock in the event of default on the note. In terms of risk, the executive has given nothing and is somewhat in the same position as the optionee. If the stock value drops, he or she may walk away from the deal with no personal risk. According to IRS regulations, the deal may be viewed as an option arrangement. Application of the IRS regulation would give the executive ordinary taxable income when the stock is purchased if the value of the stock at the time of purchase exceeds the purchase price. For example, on July 1, 1994, a corporation sells 100 shares of its stock to an executive. The stock has a fair market value on that date of $25,000 and the executive executes a nonrecourse note secured by the stock in that amount, plus 8% annual interest. He is required by the note to make an annual payment of $5,000 of principal, plus interest, beginning the following year. In 1995, the executive pays the interest on the note but no principal. He also collects dividends and votes the stock. In 1996, when the stock has appreciated in value to $30,000, the executive pays off the note. Under the IRS regulation, the executive would realize ordinary income upon payment of the nonrecourse note to the extent of the difference between the amount paid ($25,000 in 1996) and the value of the stock ($30,000).

Restricted stock. Stock subject to restrictions is taxed as pay in the first year in which it is either transferable or not subject to a substantial risk of forfeiture. A risk of forfeiture exists where your rights are conditioned upon the future performance of substantial services. Generally, taxable income is the difference between the amount, if any, that you pay for the stock and its value at the time the risk of forfeiture is removed. The valuation at the time the forfeiture restrictions lapse is not reduced because of restrictions imposed on the right to sell the property. However, restrictions which will never lapse do affect valuation.

SEC restrictions on insider trading are considered a substantial risk of forfeiture, so that there is no tax on the receipt of stock subject to such restrictions. However, the SEC now permits insiders to immediately resell stock acquired through exercise of an option granted at least six months earlier. As the stock acquired through such options is not subject to SEC restrictions, the executive is subject to immediate tax.

If the stock is subject to a restriction on transfer to comply with SEC pooling-of-interests accounting rules, the stock is considered to be subject to a substantial restriction.

Electing Immediate Tax on Restricted Stock

You may elect to be taxed on the unrestricted value of the stock at the time you receive it, less any payment you made, instead of in the year it becomes substantially vested. If you make the election, you are treated as an investor and later appreciation in value is not taxed as pay when your rights to the stock become vested. If you later forfeit the stock, a capital loss is allowed for your cost, minus any amount realized on the forfeiture. The election must generally be made by filing a statement with the IRS not later than 30 days after the date of the stock transfer.

The restricted stock rule is not restricted to compensation of employees; it may apply to any type of fee arrangement for services.

¶2.18 Educational Benefits for Employees' Children

Private foundations. The IRS has published guidelines under which a private foundation established by an employer may make tax-free grants to children of employees. An objective, nondiscriminatory program must be adopted. If the guidelines are satisfied, employees are not taxable on the benefits provided their children. Advance approval of the grant program must be obtained from the IRS.

IRS guidelines require:

- Grant recipients must be selected by a scholarship committee which is independent of the employer and the foundation. Former employees of the employer or the foundation are not considered independent.
- Eligibility for the grants may be restricted to children of employees who have been employed for a minimum of up to three years, but eligibility may not be related to the employee's position, services, or duties.
- Once awarded, a grant may not be terminated if the parent leaves his job with the employer, regardless of the reason for the termination of employment. If a one-year grant is awarded or a multi-year grant is awarded subject to renewal, a child who reapplies for a later grant may not be considered ineligible because his parent no longer works for the employer.
- Grant recipients must be based solely upon objective standards unrelated to the employer's business and the parent's employment such as prior academic performance, aptitude tests, recommendations from instructors, financial needs, and conclusions drawn from personal interviews.
- Recipients must be free to use the grants for courses which are not of particular benefit to the employer or the foundation.
- The grant program must not be used by the foundation or employer to recruit employees or induce employees to continue employment.
- There must be no requirement or suggestion that the child or parent is expected to render future employment services.

The grant program must also meet a percentage test. The number of grants awarded in a given year to children of employees must not exceed (1) 25% of the number of employees' children who were eligible, applied for the grants, and were considered by the selection committee in that year; or (2) 10% of the number of employees' children who were eligible during that year, whether or not they applied. Renewals of grants are not considered in determining the number of grants awarded.

If all guidelines other than the percentage test are satisfied, the IRS will determine whether the primary purpose of the program is to educate the children. If it is, the grants will be considered tax-free scholarships or fellowships; if it is not, the grants are taxed to the parent-employee as extra compensation.

Educational benefit trusts and other plans. A medical professional corporation set up an educational benefit plan to provide the payment of college costs to the children of "key" employees. The plan defined a key employee as an employee who was salaried at over $15,000. To receive benefits, the child must have been a candidate for a degree within two years after graduating from high school. If an eligible employee quit for reasons other than death or permanent disability, his or her children could no longer receive benefits except for expenses actually incurred before termination. The company made annual contributions to the trust for which a bank was trustee. According to the IRS, amounts contributed to the trust are a form of pay to qualified employees, as they are contributed on the basis of employment and earnings record, rather than on the basis of competitive standards such as need, merit, or motivation. However, employees are not currently taxable. The right to have their children receive benefits is conditioned upon each employee's future performance of services. Furthermore, there is a substantial risk of forfeiture. Tax is not incurred until a child has a vested right to receive benefits; here, vesting does not occur until a child becomes a candidate for a degree at an educational institution, has actually incurred educational expenses, and his or her parent is employed by the company. Once the right to receive a distribution from the plan becomes vested, the parent of the child who has incurred the expenses is taxable on the amount of the distribution. The company may then claim a deduction for the amount reported as income by the employee.

The Tax Court and appeals court have upheld the IRS position in similar plans.